

**Report of the
PUBLIC EMPLOYEE RETIREMENT
ADMINISTRATION COMMISSION
on the Examination of the
Massachusetts Housing Finance Agency
Contributory Retirement System
For the Four Year Period
January 1, 1998 - December 31, 2001
PERAC 01: 08-054-12**

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March 21, 2003

The Public Employee Retirement Administration Commission has completed an examination of the **Massachusetts Housing Finance Agency** Retirement System pursuant to G.L. c. 32, § 21. The examination covered the period from January 1, **1998** to December 31, **2001**. This audit was conducted in accordance with the accounting and management standards established by the Public Employee Retirement Administration Commission in regulation 840 CMR 25.00. Additionally, all supplementary regulations approved by PERAC and on file at PERAC are listed in this report.

In our opinion, the financial records and management functions are being performed in conformity with the standards established by the Public Employee Retirement Administration Commission with the exception of those noted in the findings presented in this report.

In closing, I acknowledge the work of examiner James Sweeney who conducted this examination and express appreciation to the Board of Retirement and staff for their courtesy and cooperation.

Sincerely,

Joseph E. Connarton
Executive Director

Massachusetts Housing Finance Agency Retirement System

EXPLANATION OF FINDINGS AND RECOMMENDATIONS

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

- 1) **Board Minutes:** The Board Meeting Minutes were not signed on 24 out of the 57 Meeting Minutes reviewed by the auditor. Most of these omissions occurred from 1998 to 2000. The pages of the Minutes are not pre-numbered or initialed by Board members. For the period from 1998 to 2000 the Minutes are not bound. Seven monthly meetings were cancelled due to lack of a quorum.

Recommendation: In accordance with G.L. c. 32, § 21 and PERAC regulations, the Minutes must be attested to and signed by all Board members in attendance. Pages of the Minutes must be pre-numbered or initialed by Board members and bound. G.L. c 32, § 20 (5) and CMR 25.31 require boards to meet at least once monthly.

Board Response: The administration of the Retirement System changed in October, 2000. Since that time all Board Meeting Minutes have been signed as required and the Minutes bound. Since December 2002, in accordance with your recommendation, each page of the Board Minutes has been initialed and numbered. The issue of Board attendance will be addressed to the best of the Board Members' ability. Two of the Board Members travel extensively on business matters and this presents problems if a third Board Member has a conflicting engagement.

- 2) **Warrants:** Monthly expense warrants were not signed by two designated persons on 17 out of 48 warrants reviewed. The Board does not generate a warrant for monthly pension payments.

Recommendation: G.L. c 32, § 23 (2) (a) states that disbursements of funds must be authorized by vote of the Board. The Board uses the warrant in lieu of a voucher system; therefore, the warrant should be signed by two persons designated by the Board.

Board Response: All Board warrants since October, 2000 have been signed in accordance with PERAC requirements and the Retirement System will be diligent in seeing this task is properly performed. A warrant for monthly pension payments has been added to the monthly warrants list since December, 2002.

- 3) **Refunds and Transfers:** The auditor found that the files for 18% of the refunds sampled contained insufficient information to determine if the transactions were correct. Interest refunded under G.L. c 32, § 11 (1) could not be ascertained from the information contained in the files. Three of the transfers files sampled could not be located.

Recommendation: The Board must receive a Withdrawal Notice form signed by an authorized individual, indicating whether the termination is voluntary or involuntary and date of termination. Members annuity savings cards must be kept up to date including transfer-in amounts from other systems, and filed with members required documentation.

Massachusetts Housing Finance Agency Retirement System

EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

Files for active, retired, and terminated members must be maintained and adequately safeguarded.

Board Response: Procedures between the MHFA Human Resources Department and the Retirement System have been changed so that the reason for employment termination is clearly stated. Previously, notices did not clearly state if terminations were voluntarily or involuntary. To the best of our knowledge no employee involuntarily terminated was denied interest due to this notice issue.

Prior to and during the audit, this Retirement System's files were in the process of being reorganized to cure problems with inadequate file maintenance. This issue had already been recognized by staff prior to the audit and steps taken to cure the problem.

- 4) **Members' Deduction Rates:** The auditor sampled over 10% of members' deduction rates to determine that correct percentages are being withheld and that the additional 2% deduction is withheld from those members who earn over \$30,000 and were hired after January 1, 1979. The sample yielded a 23% error rate. There were 9 members with the wrong deduction rate being withheld and 2 members earning over \$30,000 who were not having the additional 2% withheld.

Recommendation: The deduction errors found must be corrected by the Board and agency payroll department. The Board needs to routinely monitor deductions to ensure compliance with G.L. c 32, § 22 (1) (b) and (1) (b1/2).

Board Response: The incorrect deduction rates have been corrected. A plan to recoup amounts not correctly deducted is now being drafted and will be implemented by April 1, 2003 upon Board approval. Most of the errors in the deduction rates occurred with employees hired in 1996 and 1997 when the MHFA payroll system was changed from an outside vendor to in-house staff. There is now a process in place between the Retirement System and Payroll system to ensure all new employees have appropriate deductions made. Monthly internal audits are undertaken to ensure the process is correctly implemented.

This Retirement System, however, takes issue with the characterization of the sample as indicating a 23% error rate, which implies that error rate was applicable to all active retirement members. This is not correct. The auditor's sample to the best of my knowledge was not entirely a random sample. I believe the auditor initially went through the MHFA payroll run and selected a number of employees who appeared on first impression to have the wrong deductions being made on the basis of their employment date. He also may have selected some employees randomly to include in this selection list.

Massachusetts Housing Finance Agency Retirement System

EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

After the exit interview in which the deduction rate problem was raised, I audited all the active member files and from 325 files uncovered only two more employees with an incorrect deduction rate. Thus with the 11 errors the auditor found and the two additional I discovered, the total employees with incorrect rates equaled 13 out of 325 employees or a 4% rate. Although errors of this type do occasionally occur, a 4% error rate is still unacceptable and the errors identified have been corrected.

- 5) **Trial Balance:** Pre-closing trial balances for December 31, 1999, 2000 and 2001 were not saved. Pre-closing trial balances are required to trace closing entries through to the post-closing trial balance. The Board is using a computer aided manual system for accounting and membership and neither hard copies nor computer files were saved.

Recommendation: The Boards must comply with 840 CMR 4.01, and Retirement Board Records Disposal Schedule (DS-17-90) as prescribed by The Office of the Secretary of State.

Board Response: The Board fully accepts your recommendations and will implement them immediately.

- 6) **Annual Statement:** Based upon inspection of the Annual Statements filed by the Board for the four year audit period, it was determined that certain line item amounts contained in the Annual Statement did not match the detailed supporting schedules. Differences were found in cash, equities, and pooled funds.

Recommendation: As a sole source of information to third parties, the Annual Statement and supporting schedules must be able to stand on their own without having to reference the general ledger. Prior to submission of the Annual Statement, a review process should be established to ensure all entries on the Annual Statement agree with the detailed supporting schedules using the PERAC Annual Statement Guide published each year. If necessary, differences in custodian provided schedules should be reconciled to the amounts reported in the statement.

Board Response: This issue arose because the custodial access to certain investments by our real estate managers and alternative investment manager is not always available to the custodian when the custodian issues its report. Additionally, two cash checking accounts and one brokerage account with a stock distribution are outside the custodian's control. The Retirement System will, however, comply with your recommendation and consolidate the present financial information for the Annual Statement.

Massachusetts Housing Finance Agency Retirement System

EXPLANATION OF FINDINGS AND RECOMMENDATIONS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

- 7) **Cash Reconciliation:** The agency treasurer is not performing a reconciliation of the retirement system's cash accounts on a monthly basis as required as custodian of the system's funds.

Recommendation

The Agency Treasurer or his designee shall be the custodian of the retirement systems funds according to G.L. c 32, § 23 (2) (a). Regulation 840 CMR 25.13(6) states that the Treasurer must perform a monthly reconciliation of the cash accounts of the retirement system as part of his/her custodial duties.

The Board must require that the treasurer, or designee perform his/her statutory obligation as custodian of the funds, the designee must not be a Board member or staff member to ensure segregation of duties and adequate internal controls.

Board Response: The Retirement System Treasurer has at the February 11, 2003 meeting of the Retirement Board designated the Comptroller of the MHFA, who is neither a Retirement System Board nor staff member, to reconcile on a monthly basis the Retirement System's cash accounts in accordance with PERAC's recommendation.

- 8) **Members' Deposit Control Cards:** The Board is not maintaining individual members' accounts.

Recommendation: Member contributions must be posted to the individual accounts on a regular basis, and interest credited to the account annually according to 840 CMR 25.32 (14) and (16).

Board Response: This Retirement System is unclear as to this comment and recommendation. Members' contributions are posted weekly to their accounts, both in the Retirement System's computer system and the MHFA payroll system. Manual posting to deposit control cards is not done in light of the dual computer posting, both systems which have backups to protect the data. Interest is credited annually and notices thereof distributed annually. We believe this system complied with PERAC requirements but are willing to discuss this further to clear any confusion on our part.

Final Determination

PERAC auditors will follow-up in six (6) months to ensure that appropriate action has been taken regarding the audit findings.

Massachusetts Housing Finance Agency Retirement System

STATEMENT OF LEDGER ASSETS AND LIABILITIES

**FOR THE FOUR YEAR PERIOD BEGINNING JANUARY 1, 1998
AND ENDING DECEMBER 31, 2001**

	FOR THE PERIOD ENDING DECEMBER 31,			
ASSETS	2001	2000	1999	1998
Cash	\$1,174,989	\$754,421	\$941,111	\$4,584,689
Short Term Investments	0	0	0	0
Fixed Income Securities (at book value)	15,991,323	14,787,559	13,998,208	13,658,456
Equities	15,686,389	17,662,478	20,562,865	17,179,830
Pooled Short Term Funds	0	0	0	0
Pooled Domestic Equity Funds	0	0	0	0
Pooled International Equity Funds	0	0	0	0
Pooled Global Equity Funds	0	0	0	0
Pooled Domestic Fixed Income Funds	0	0	0	0
Pooled International Fixed Income Funds	0	0	0	0
Pooled Global Fixed Income Funds	3,263,455	3,855,239	3,685,276	0
Pooled Alternative Investment Funds	1,105,186	1,711,238	1,047,715	483,935
Pooled Real Estate Funds	3,050,080	2,808,661	2,374,799	1,566,667
Pooled Domestic Balanced Funds	0	0	0	0
Pooled International Balanced Funds	0	0	0	0
PRIT Cash Fund	0	0	0	0
PRIT Core Fund	0	0	0	0
Interest Due and Accrued	178,079	164,679	147,541	129,813
Accounts Receivable	329,633	5,033	6,033	5,112
Accounts Payable	(523,800)	(2,930)	(470)	(470)
TOTAL	<u>\$40,255,334</u>	<u>\$41,746,380</u>	<u>\$42,763,078</u>	<u>\$37,608,033</u>
FUND BALANCES				
Annuity Savings Fund	\$13,746,083	\$12,935,673	\$11,644,721	\$10,531,407
Annuity Reserve Fund	2,907,011	2,367,687	2,277,000	2,281,098
Pension Fund	4,103,069	4,971,133	5,837,698	6,583,035
Military Service Fund	0	0	0	0
Expense Fund	0	0	0	0
Pension Reserve Fund	19,499,171	21,471,886	23,003,659	18,212,493
TOTAL	<u>\$40,255,334</u>	<u>\$41,746,380</u>	<u>\$42,763,078</u>	<u>\$37,608,033</u>

Massachusetts Housing Finance Agency Retirement System

STATEMENT OF CHANGES IN FUND BALANCES

**FOR THE FOUR YEAR PERIOD BEGINNING JANUARY 1, 1998
AND ENDING DECEMBER 31, 2001**

	Annuity Savings Fund	Annuity Reserve Fund	Pension Fund	Military Service Fund	Expense Fund	Pension Reserve Fund	Total All Funds
Beginning Balance (1998)	\$9,768,726	\$2,091,147	\$6,631,885	\$0	\$143,104	\$12,575,558	\$31,210,421
Receipts	1,643,581	64,442	188,748	0	94,099	6,246,498	8,237,368
Interfund Transfers	(341,987)	341,987	609,563	0	0	(609,563)	0
Disbursements	(538,913)	(216,477)	(847,162)	0	(237,203)	0	(1,839,756)
Ending Balance (1998)	10,531,407	2,281,098	6,583,035	0	0	18,212,493	37,608,033
Receipts	1,703,314	67,130	139,484	0	383,975	4,791,166	7,085,070
Interfund Transfers	(158,040)	158,040	0	0	0	0	0
Disbursements	(431,960)	(229,268)	(884,821)	0	(383,975)	0	(1,930,025)
Ending Balance (1999)	11,644,721	2,277,000	5,837,698	0	0	23,003,659	42,763,078
Receipts	1,854,837	67,298	69,326	0	671,213	(1,531,773)	1,130,901
Interfund Transfers	(259,762)	259,762	0	0	0	0	0
Disbursements	(304,123)	(236,373)	(935,891)	0	(671,213)	0	(2,147,600)
Ending Balance (2000)	12,935,673	2,367,687	4,971,133	0	0	21,471,886	41,746,380
Receipts	2,019,583	79,366	206,535	0	520,741	(1,972,715)	853,510
Interfund Transfers	(748,954)	748,954	0	0	0	0	0
Disbursements	(460,220)	(288,995)	(1,074,600)	0	(520,741)	0	(2,344,556)
Ending Balance (2001)	<u>\$13,746,083</u>	<u>\$2,907,011</u>	<u>\$4,103,069</u>	<u>\$0</u>	<u>\$0</u>	<u>\$19,499,171</u>	<u>\$40,255,334</u>

Massachusetts Housing Finance Agency Retirement System

STATEMENT OF INCOME

**FOR THE FOUR YEAR PERIOD BEGINNING JANUARY 1, 1998
AND ENDING DECEMBER 31, 2001**

	FOR THE PERIOD ENDING DECEMBER 31,			
	2001	2000	1999	1998
Annuity Savings Fund:				
Members Deductions	\$1,645,036	\$1,506,334	\$1,397,165	\$1,295,526
Transfers from other Systems	112,571	84,615	48,642	28,397
Member Make Up Payments and Redeposits	27,239	25,117	30,583	95,154
Investment Income Credited to Member Accounts	<u>234,737</u>	<u>238,771</u>	<u>226,924</u>	<u>224,504</u>
Sub Total	<u>2,019,583</u>	<u>1,854,837</u>	<u>1,703,314</u>	<u>1,643,581</u>
Annuity Reserve Fund:				
Investment Income Credited Annuity Reserve Fund	<u>79,366</u>	<u>67,298</u>	<u>67,130</u>	<u>64,442</u>
Pension Fund:				
3 (8) (c) Reimbursements from Other Systems	206,535	69,326	139,484	188,748
Received from Commonwealth for COLA and				
Survivor Benefits	0	0	0	0
Pension Fund Appropriation	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Sub Total	<u>206,535</u>	<u>69,326</u>	<u>139,484</u>	<u>188,748</u>
Military Service Fund:				
Contribution Received from Municipality on Account				
of Military Service	0	0	0	0
Investment Income Credited Military Service Fund	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Sub Total	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Expense Fund:				
Expense Fund Appropriation	0	0	0	0
Investment Income Credited to Expense Fund	<u>520,741</u>	<u>671,213</u>	<u>383,975</u>	<u>94,099</u>
Sub Total	<u>520,741</u>	<u>671,213</u>	<u>383,975</u>	<u>94,099</u>
Pension Reserve Fund:				
Federal Grant Reimbursement	0	0	0	0
Pension Reserve Appropriation	0	0	0	0
Interest Not Refunded	4,186	11,410	2,528	12,398
Excess Investment Income	<u>(1,976,901)</u>	<u>(1,543,183)</u>	<u>4,788,638</u>	<u>6,234,100</u>
Sub Total	<u>(1,972,715)</u>	<u>(1,531,773)</u>	<u>4,791,166</u>	<u>6,246,498</u>
TOTAL RECEIPTS	<u>\$853,510</u>	<u>\$1,130,901</u>	<u>\$7,085,070</u>	<u>\$8,237,368</u>

Massachusetts Housing Finance Agency Retirement System

STATEMENT OF DISBURSEMENTS

**FOR THE FOUR YEAR PERIOD BEGINNING JANUARY 1, 1998
AND ENDING DECEMBER 31, 2001**

	FOR THE PERIOD ENDING DECEMBER 31,			
	2001	2000	1999	1998
Annuity Savings Fund:				
Refunds to Members	\$390,078	\$290,169	\$214,969	\$462,270
Transfers to other Systems	<u>70,142</u>	<u>13,953</u>	<u>216,991</u>	<u>76,643</u>
Sub Total	<u>460,220</u>	<u>304,123</u>	<u>431,960</u>	<u>538,913</u>
Annuity Reserve Fund:				
Annuities Paid	288,995	236,373	229,268	216,477
Option B Refunds	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Sub Total	<u>288,995</u>	<u>236,373</u>	<u>229,268</u>	<u>216,477</u>
Pension Fund:				
Pensions Paid				
Regular Pension Payments	980,434	825,423	800,254	756,728
Survivorship Payments	11,580	11,242	6,833	12,805
Ordinary Disability Payments	13,370	12,981	12,621	12,417
Accidental Disability Payments	66,554	65,834	65,114	64,706
Accidental Death Payments	0	0	0	0
Section 101 Benefits	0	0	0	0
3 (8) (c) Reimbursements to Other Systems	2,663	20,412	0	507
State Reimbursable COLA's Paid	0	0	0	0
Chapter 389 Beneficiary Increase Paid	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Sub Total	<u>1,074,600</u>	<u>935,891</u>	<u>884,821</u>	<u>847,162</u>
Military Service Fund:				
Return to Municipality for Members Who				
Withdrew Their Funds	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Expense Fund:				
Board Member Stipend	14,500	13,750	15,000	0
Salaries	159,259	262,812	115,415	30,656
Legal Expenses	0	0	0	0
Medical Expenses	0	0	0	0
Travel Expenses	6,146	8,802	4,122	12,053
Administrative Expenses	25,504	45,168	26,821	12,209
Furniture and Equipment	0	0	0	0
Management Fees	255,470	268,915	173,037	133,658
Custodial Fees	37,362	42,099	37,205	31,913
Consultant Fees	<u>22,500</u>	<u>29,667</u>	<u>12,375</u>	<u>16,714</u>
Sub Total	<u>520,741</u>	<u>671,213</u>	<u>383,975</u>	<u>237,203</u>
TOTAL DISBURSEMENTS	<u>\$2,344,556</u>	<u>\$2,147,600</u>	<u>\$1,930,025</u>	<u>\$1,839,756</u>

Massachusetts Housing Finance Agency Retirement System

INVESTMENT INCOME

**FOR THE FOUR YEAR PERIOD BEGINNING JANUARY 1, 1998
AND ENDING DECEMBER 31, 2001**

	FOR THE PERIOD ENDING DECEMBER 31,			
	2001	2000	1999	1998
Investment Income Received From:				
Cash	26042.74	35231.76	\$54,734	\$49,542
Short Term Investments	3,539	5,592	-	-
Fixed Income	1,007,251	950,176	889,647	1,255,485
Equities	198,183	214,087	256,713	183,871
Pooled or Mutual Funds	<u>182,210</u>	<u>189,900</u>	<u>180,791</u>	<u>80,032</u>
Commission Recapture	<u>7,274</u>	<u>9,314</u>	<u>10,160</u>	<u>5,062</u>
TOTAL INVESTMENT INCOME	<u>1,424,499</u>	<u>1,404,301</u>	<u>1,392,044</u>	<u>1,573,991</u>
Plus:				
Increase in Amortization of Fixed Income Securities	238,894	611,964	29,045	12,767
Realized Gains	1,978,277	2,693,258	3,090,937	2,534,216
Unrealized Gains	656,350	2,340,203	3,448,495	4,251,569
Interest Due and Accrued on Fixed Income Securities - Current Year	<u>178,079</u>	<u>164,679</u>	<u>147,541</u>	<u>129,813</u>
Sub Total	<u>3,051,600</u>	<u>5,810,104</u>	<u>6,716,017</u>	<u>6,928,366</u>
Less:				
Decrease in Amortization of Fixed Income Securities	(382)	-	(614,348)	(11,301)
Paid Accrued Interest on Fixed Income Securities	(44,740)	(13,906)	(46,398)	(71,069)
Realized Loss	(3,864,190)	(3,253,106)	(1,850,834)	(1,677,667)
Unrealized Loss	(1,544,165)	(4,365,752)	-	(4,239)
Custodial Fees Paid	-	-	-	-
Consultant Fees Paid	-	-	-	-
Management Fees Paid	-	-	-	-
Board Member Stipend	-	-	-	-
Interest Due and Accrued on Fixed Income Securities - Prior Year	<u>(164,679)</u>	<u>(147,541)</u>	<u>(129,813)</u>	<u>(120,947)</u>
Sub Total	<u>(5,618,157)</u>	<u>(7,780,305)</u>	<u>(2,641,394)</u>	<u>(1,885,223)</u>
NET INVESTMENT INCOME	<u>(1,142,058)</u>	<u>(565,901)</u>	<u>5,466,668</u>	<u>6,617,134</u>
Income Required:				
Annuity Savings Fund	234,737	238,771	226,924	224,504
Annuity Reserve Fund	79,366	67,298	67,130	64,442
Military Service Fund	-	-	-	-
Expense Fund	<u>520,741</u>	<u>671,213</u>	<u>383,975</u>	<u>94,099</u>
TOTAL INCOME REQUIRED	<u>834,844</u>	<u>977,282</u>	<u>678,029</u>	<u>383,044</u>
Net Investment Income	<u>(1,142,058)</u>	<u>(565,901)</u>	<u>5,466,668</u>	<u>6,617,134</u>
Less: Total Income Required	<u>834,844</u>	<u>977,282</u>	<u>678,029</u>	<u>383,044</u>
EXCESS INCOME TO THE PENSION RESERVE FUND	<u>(\$1,976,901)</u>	<u>(\$1,543,183)</u>	<u>\$4,788,638</u>	<u>\$6,234,090</u>

Massachusetts Housing Finance Agency Retirement System

STATEMENT OF ALLOCATION OF INVESTMENTS OWNED

(percentages by category)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

	BOOK VALUE*	MARKET VALUE	PERCENTAGE OF TOTAL ASSETS	PERCENTAGE ALLOWED*
Cash		\$1,174,989	2.92%	100
Short Term			0.00%	100
Fixed Income		15,991,323	39.71%	40 - 80
Equities		15,686,389	38.95%	40
Pooled Short Term Funds			0.00%	
Pooled Domestic Equity Funds			0.00%	
Pooled International Equity Funds			0.00%	
Pooled Global Equity Funds			0.00%	
Pooled Domestic Fixed Income Funds			0.00%	
Pooled International Fixed Income Funds			0.00%	
Pooled Global Fixed Income Funds			0.00%	
Pooled Alternative Investment Funds		1,105,186	2.74%	5
Pooled Real Estate Funds		3,050,080	7.57%	5**
Pooled Domestic Balanced Funds			0.00%	
Pooled International Balanced Funds		3,263,455	8.10%	
PRIT Cash Fund			0.00%	
PRIT Core Fund			0.00%	100
GRAND TOTALS	\$0	<u>\$40,271,422</u>	<u>100.00%</u>	

** The Pooled Real estate Funds were less than 5% of total market value of the portfolio at the time of investment.

* The book value differs from the market value for individually owned Fixed Income Securities which are valued at amortized cost which is the original cost of the investment plus or minus any bond discount or bond premium calculated ratably to maturity. All other investments are reflected at their quoted market value.

For the year ending December 31, **2001**, the rate of return for the investments of the **Massachusetts Housing Finance Agency** Retirement System was -2.93%. For the five year period ending December 31, **2001**, the rate of return for the investments of the **Massachusetts Housing Finance Agency** Retirement System averaged 9.46%. For the 17-year period ending December 31, **2001**, since PERAC began evaluating the returns of the retirement systems, the rate of return of the investments of the **Massachusetts Housing Finance Agency** Retirement System was 9.05%.

Massachusetts Housing Finance Agency Retirement System

SUPPLEMENTARY INVESTMENT REGULATIONS

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

The **Massachusetts Housing Finance Agency** Retirement System submitted the following supplementary investment regulations, which were approved by PERAC on:

March 14, 1996

- 20.09(1) Venture capital investments shall not exceed 3% of the total market value of the portfolio at the time of investment provided that in any system with assets in excess of nineteen million dollars, venture capital investments may be made up to an amount equal to 5% of the total market value of the portfolio at the time of investment, shall be considered a separate asset class, and provided further that:
- (a) the board does not participate in the selection of the personnel responsible for making venture capital investments or otherwise exercise discretion in business affairs and should this be required, prior to any participation by the board, the board shall consult with PERA to determine the appropriate course of action;
 - (b) such personnel retain authority in the decision making process, and
 - (c) should an investment in venture capital result in the direct ownership of securities, such shall be permitted only until such time as divestiture is prudent.
- 20.09(2) Venture capital investments shall only be made in venture capital funds operated by venture capital firms having their principal places of business in the United States.
- 20.09(3) All venture capital investments shall be made in companies which have their principal places of business in the United States.

October 5, 1999

- 16.08 In accordance with PERAC Investment Guideline 99-3, the Massachusetts Housing Finance Authority Retirement Board may invest in Ascent Venture Partners III, L.P. The system is an investor in Ascent Partners II, L.P. and has submitted the required documentation to justify investing in Ascent Venture Partners III.

Massachusetts Housing Finance Agency Retirement System

NOTES TO FINANCIAL STATEMENTS

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

NOTE 1 - THE SYSTEM

The plan is a contributory defined benefit plan covering all **Massachusetts Housing Finance Agency** Retirement System member unit employees deemed eligible by the retirement board, with the exception of school department employees who serve in a teaching capacity. The Teachers' Retirement Board administers the pensions of such school employees.

Instituted in 1937, the System is a member of the Massachusetts Contributory Retirement System and is governed by Chapter 32 of the Massachusetts General Laws. Membership in the plan is mandatory immediately upon the commencement of employment for all permanent, full-time employees.

The system provides for retirement allowance benefits up to a maximum of 80% of a member's highest three year average annual rate of regular compensation. Benefit payments are based upon a member's age, length of creditable service, level of compensation, and group classification.

Members become vested after ten years of creditable service. A superannuation retirement allowance may be received upon the completion of twenty years of service or upon reaching the age of 55 with ten years of service. Normal retirement for most employees occurs at age 65 (for certain hazardous duty and public safety positions, normal retirement is at age 55).

A retirement allowance consists of two parts: an annuity and a pension. A member's accumulated total deductions and a portion of the interest they generate constitute the annuity. The differential between the total retirement benefit and the annuity is the pension. The average retirement benefit is approximately 75 - 85% pension and 15 - 25% annuity.

Active members contribute either 5, 7, 8, or 9% of their gross regular compensation. Members joining the retirement system after January 1, 1979 must contribute an additional 2% on regular compensation earned at a rate in excess of \$30,000. The percentage rate is keyed to the date upon which an employee's membership commences. These deductions are deposited in the Annuity Savings Fund and earn interest at a rate determined by the Executive Director of PERAC according to statute. When a member's retirement becomes effective, his/her deductions and related interest are transferred to the Annuity Reserve Fund. Any cost-of-living adjustment granted between 1981 and 1997 and any increase in other benefits imposed by state law during that period are borne by the state.

The pension portion of any retirement benefit is paid from the Pension Fund of the System. The governmental unit employing the member must annually appropriate and contribute the amount of current year pension payments as indicated on the most recent funding schedule as approved by PERAC's Actuary. Until recently, retirement systems were paying only the actual retirement

Massachusetts Housing Finance Agency Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

benefits that were due each year. Systems had no statutory authorization to put aside any money for the future benefits of employees who are now working. Large unfunded liabilities resulted from operating upon this pay-as-you-go basis. In 1977, legislation authorized local governments to appropriate funds to meet future pension obligations.

In 1983, additional legislation was passed requiring the transfer of investment earnings (in excess of the amount credited to member accounts) into the Pension Reserve Fund. These initiatives have significantly reduced the rate of growth of the retirement systems' unfunded liabilities, and in some systems have actually eliminated such liability.

Administrative expenses are funded through investment income of the system.

Members who become permanently and totally disabled for further duty may be eligible to receive a disability retirement allowance. The amount of benefits to be received in such cases is dependent upon several factors including: whether or not the disability is work related, the member's age, years of creditable service, level of compensation, veteran's status, and group classification.

Employees who resign from service and who are not eligible to receive a retirement allowance or are under the age of 55 are entitled to request a refund of their accumulated total deductions. In addition, depending upon the number of years of creditable service, such employees are entitled to receive either zero (0%) percent, fifty (50%) percent, or one hundred (100%) percent of the regular interest which has accrued upon those deductions. Survivor benefits are extended to eligible beneficiaries of members whose death occurs prior to or following retirement.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

The accounting records of the System are maintained on a calendar year basis in accordance with the standards and procedures established by the Executive Director of Public Employee Retirement Administration Commission.

The Annuity Savings Fund is the fund in which members' contributions are deposited. Active members contribute either 5, 7, 8, or 9% of their gross regular compensation. Voluntary contributions, redeposits, and transfers to and from other systems, are also accounted for in this fund. Members' contributions to the fund earn interest at a rate determined by PERAC. Interest for some members who withdraw with less than ten years of service is transferred to the Pension Reserve Fund. Upon retirement, members' contributions and interest are transferred to the Annuity Reserve Fund. Dormant account balances must be transferred to the Pension Reserve Fund after a period of ten years of inactivity.

Massachusetts Housing Finance Agency Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

The Annuity Reserve Fund is the fund to which a member's account is transferred upon retirement from the Annuity Savings Fund and Special Military Service Credit Fund. The annuity portion of the retirement allowance is paid from this fund. Interest is credited monthly to this fund at the rate of 3% annually on the previous month's balance.

The Special Military Service Credit Fund contains contributions and interest for members while on a military leave for service in the Armed Forces who will receive creditable service for the period of that leave.

The Expense Fund contains amounts transferred from investment income for the purposes of administering the retirement system.

The Pension Fund contains the amounts appropriated by the governmental units as established by PERAC to pay the pension portion of each retirement allowance.

The Pension Reserve Fund contains amounts appropriated by the governmental units for the purposes of funding future retirement benefits. Any profit or loss realized on the sale or maturity of any investment or on the unrealized gain of a market valued investment as of the valuation date is credited to the Pension Reserve Fund. Additionally, any investment income in excess of the amount required to credit interest to the Annuity Savings Fund, Annuity Reserve Fund, and Special Military Service Credit Fund is credited to this Reserve account.

The Investment Income Account is credited with all income derived from interest and dividends of invested funds. At year-end the interest credited to the Annuity Savings Fund, Annuity Reserve Fund, Expense Fund, and Special Military Service Credit Fund is distributed from this account and the remaining balance is transferred to the Pension Reserve Fund.

NOTE 3 - SUPPLEMENTARY MEMBERSHIP REGULATIONS

The **Massachusetts Housing Finance Agency** Retirement System has not submitted any supplementary membership regulations to PERAC.

Massachusetts Housing Finance Agency Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

NOTE 4 - ADMINISTRATION OF THE SYSTEM

The System is administered by a five person Board of Retirement consisting of the Treasurer who shall be a member ex officio, a second member appointed by the governing authority, a third and fourth member who shall be elected by the members in or retired from the service of such system, and a fifth member appointed by the other four board members.

Ex officio Member: Andris Silinis

Appointed Member: Christopher Johnson Term Expires 11/12/05

Elected Member: Michael Fitzmaurice Term Expires: 12/8/04

Elected Member: Katherine King Term Expires: 6/30/03

Appointed Member: Paul T. Hynes Term Expires: 12/12/05

The Board members are required to meet at least once a month. The Board must keep a record of all of its proceedings. The Board must annually submit to the appropriate authority an estimate of the expenses of administration and cost of operation of the system. The board must annually file a financial statement of condition for the system with the Executive Director of PERAC.

The investment of the system's funds is the responsibility of the Board. All retirement allowances must be approved by the Retirement Board and are then submitted to the PERAC Actuary for verification prior to payment. All expenses incurred by the System must be approved by at least two members of the Board.

The following retirement board members and employees are bonded by an authorized agent representing a company licensed to do business in Massachusetts as follows:

Treasurer - Custodian:)	
Ex officio Member:)	\$30,000,000 Fiduciary Liability
Elected Member:)	MACRS Policy
Appointed Member:)	\$1,000,000 Employee Dishonesty
Staff Employee:)	Travelers Indemnity Co.

Massachusetts Housing Finance Agency Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

NOTE 5 - ACTUARIAL VALUATION AND ASSUMPTIONS

The most recent actuarial valuation of the System was prepared by **John Hancock Financial Services, Inc.** as of **January 1, 2000**.

The actuarial liability for active members was	\$20,386,659
The actuarial liability for vested terminated members was	2,139,389
The actuarial liability for retired members was	<u>9,212,563</u>
The total actuarial liability was	31,738,611
System assets as of that date were	<u>42,763,078</u>
The unfunded actuarial liability was	<u>(\$11,024,467)</u>
 The ratio of system's assets to total actuarial liability was	 134.7%
As of that date the total covered employee payroll was	\$17,002,009

The normal cost for employees on that date was 8.40% of payroll
The normal cost for the employer was 4.80% of payroll

The principal actuarial assumptions used in the valuation are as follows:

Investment Return: 8.00% per annum
Rate of Salary Increase: 6.00% per annum

GASB STATEMENT NO. 25, DISCLOSURE INFORMATION AS OF JANUARY 1, 2000

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a % of Cov. Payroll ((b-a)/c)
1/1/2000	\$42,763,078	\$31,738,611	(\$11,024,467)	134.7%	\$17,002,008	-64.84%
1/1/1999	\$38,000,556	\$33,943,345	(\$4,057,211)	112.0%	\$15,803,835	-25.67%
1/1/1998	\$31,639,644	\$27,017,925	(\$4,621,719)	117.1%	\$14,197,650	-32.55%
1/1/1997	\$27,457,882	\$25,498,462	(\$1,959,420)	107.7%	\$17,669,365	-11.09%
1/1/1996	\$24,292,125	\$22,196,309	(\$2,095,816)	109.4%	\$16,669,212	-12.57%

Massachusetts Housing Finance Agency Retirement System

NOTES TO FINANCIAL STATEMENTS (Continued)

FOR THE FOUR YEAR PERIOD ENDING DECEMBER 31, 2001

NOTE 6 - MEMBERSHIP EXHIBIT

Retirement in Past Years	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Superannuation	0	0	8	0	4	21	5	3	4	10
Ordinary Disability	0	0	0	0	0	0	0	0	0	0
Accidental Disability	0	0	0	0	0	0	0	0	0	0
Total Retirements	0	0	8	0	4	21	5	3	4	10
Total Retirees, Beneficiaries and Survivors	18	18	26	25	28	50	53	54	56	64
Total Active Members	277	310	353	368	366	312	291	308	311	326
Pension Payments										
Superannuation	\$151,659	\$133,492	\$277,013	\$309,968	\$337,830	\$596,480	\$756,728	\$800,254	\$825,423	\$980,434
Survivor/Beneficiary Payments	5,708	12,142	12,246	0	0	19,032	12,805	6,833	11,242	11,580
Ordinary Disability	11,866	11,750	11,886	12,528	12,572	12,291	12,417	12,621	12,981	13,370
Accidental Disability	26,566	63,374	63,644	67,910	68,000	64,454	64,706	65,114	65,834	66,554
Other	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total Payments for Year	<u>\$195,799</u>	<u>\$220,758</u>	<u>\$364,789</u>	<u>\$390,406</u>	<u>\$418,402</u>	<u>\$692,257</u>	<u>\$846,655</u>	<u>\$884,821</u>	<u>\$915,479</u>	<u>\$1,071,937</u>